FYR Macedonia

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Investment Profile
2001

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EBRD ANNUAL MEETING

Contents

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Introduction

Positive achievements in the past year include sustained economic recovery and stabilisation, some important privatisations and structural reforms, new agreements with the IMF and World Bank, a significant trade agreement with the EU, new infrastructure projects under the Stability Pact and a new government programme to address poverty and further structural reform. Outstanding challenges include the need to accelerate privatisation and introduce greater liberalisation in key strategic sectors, the need to further rationalise the financial sector and to intensify action to improve the investment climate.

Recent achievements

The economy has made a strong and sustained recovery from the Kosovo crisis of 1999, with growth of over 5 per cent in 2000, the country's highest rate of growth since transition began. Demand from Kosovo for construction and building materials has been a major factor, as has easier access to EU markets thanks to the reopening of transport routes. The opening up of FR Yugoslavia, a traditional trading partner for the country, is set to help sustain growth. Macroeconomic stabilisation is successful, with inflation contained by a tight monetary policy, based on a de facto peg of the exchange rate vis-à-vis the euro. This policy has been strengthened by a significant increase in foreign reserves in 2000, now covering more than three months of imports.

Notable progress has been made in structural reforms, including the sale or closure of some loss-making state-owned enterprises and the introduction of a number of important new laws. The recent privatisation of the telecommunications monopoly, a sale that had been delayed by the Kosovo crisis, will give a positive signal to potential investors in future privatisations. Most of the 12 loss-making companies identified by the World Bank in 1999 as priorities for sale or liquidation have been sold, and a new list of 40 drawn up for sale by the end of 2002.

On 29 November 2000 the IMF announced a new three-year arrangement worth about US$ 31 million under Extended Fund Facility conditions, and in principle approved funding of about US$ 13 million under Poverty Reduction and Growth Facility conditions. The arrangement was confirmed following discussion on 14 December of the country's Interim Poverty Reduction Strategy Paper (IPRSP). At the same time a new Financial and Enterprise Sector Adjustment Loan programme was concluded with the World Bank, worth about US$ 50 million.

At a summit meeting held in Zagreb in November, the EU made a commitment to the country, along with Croatia, Bosnia and Herzegovina, FR Yugoslavia, and Albania, to help them become potential candidates for membership, in exchange for their commitment to good neighbourly relations, respect for international obligations, and an effort towards greater economic cooperation as well as joint action to fight corruption and crime. The EU pledged to give about € 4.65 billion to a new aid programme for the region from 2000-06, with further funding forthcoming when required as a result of increased regional cooperation. At the same time, the republic was the first of these countries to initial a Stabilisation and Association Agreement, paving the way for free trade with EU member states and marking the first step on the ladder towards future accession.

In July 2000, the country began formal accession negotiations with the World Trade Organisation, which should add needed impetus to trade liberalisation.

As part of the Stability Pact initiative for South-Eastern Europe, a number of infrastructure projects throughout the region are being targeted under the "Quick Start" programme, coordinated by the European Commission and the World Bank. In the republic, these projects include new roads on the east-west and north-south corridors and a programme to improve water and waste-water infrastructure (see *Major sectors of the economy* below). Funding for these programmes is being provided primarily by the EBRD, EIB and bilateral donors and the work was already under way in early 2001. The EBRD is also coordinating a private sector initiative under the Stability Pact. This initiative primarily involves support to small and medium size enterprises, including the EBRD Trade Facilitation Programme whereby the EBRD guarantees the letters of credit of local enterprises to facilitate intra-regional and international trade.

Key challenges to be met

Alongside these achievements, the country still faces a number of key transition challenges. These include the need to make further progress with the privatisation or closure of large loss-making enterprises, upon which World Bank funding is still conditional, the sale of key public monopolies in strategic sectors (such as the electricity utility), and rationalisation of the financial sector through further privatisation and consolidation. However, while unemployment is very high, there is reluctance to increase it through the closure or restructuring of loss-making companies.

If the country is to attract further foreign investment, improvements to the investment climate must be made to reduce bureaucratic obstacles and inconsistencies in the legislation. Significant foreign investment in future large-scale privatisation transactions would strengthen ownership and enterprise performance. Faster action is needed to stimulate competition, such as liberalisation of the telecommunications sector, now that a majority stake in the state monopoly has been sold to a foreign investor. Despite the pace of economic growth, enterprise sector performance is slow, with substantial inter-enterprise arrears. This is partly due to extensive privatisation through management-employee buy-outs, the absence of hard budget constraints and effective bankruptcy procedures and weak enforcement of creditor and shareholder rights.

Another obstacle to enterprise development is a lack of working capital (which affects small and medium-sized enterprises in particular), as well as restrictive labour laws and high labour taxes which discourage enterprises from expanding employment – while unemployment is very high, at over 30 per cent of the labour force. A significant reduction in labour taxes during 2001 is a key target under the new IMF and World Bank programmes. The government has recently reduced personal income tax rates and VAT in a move to boost the private sector and employment.

Government programme of reform

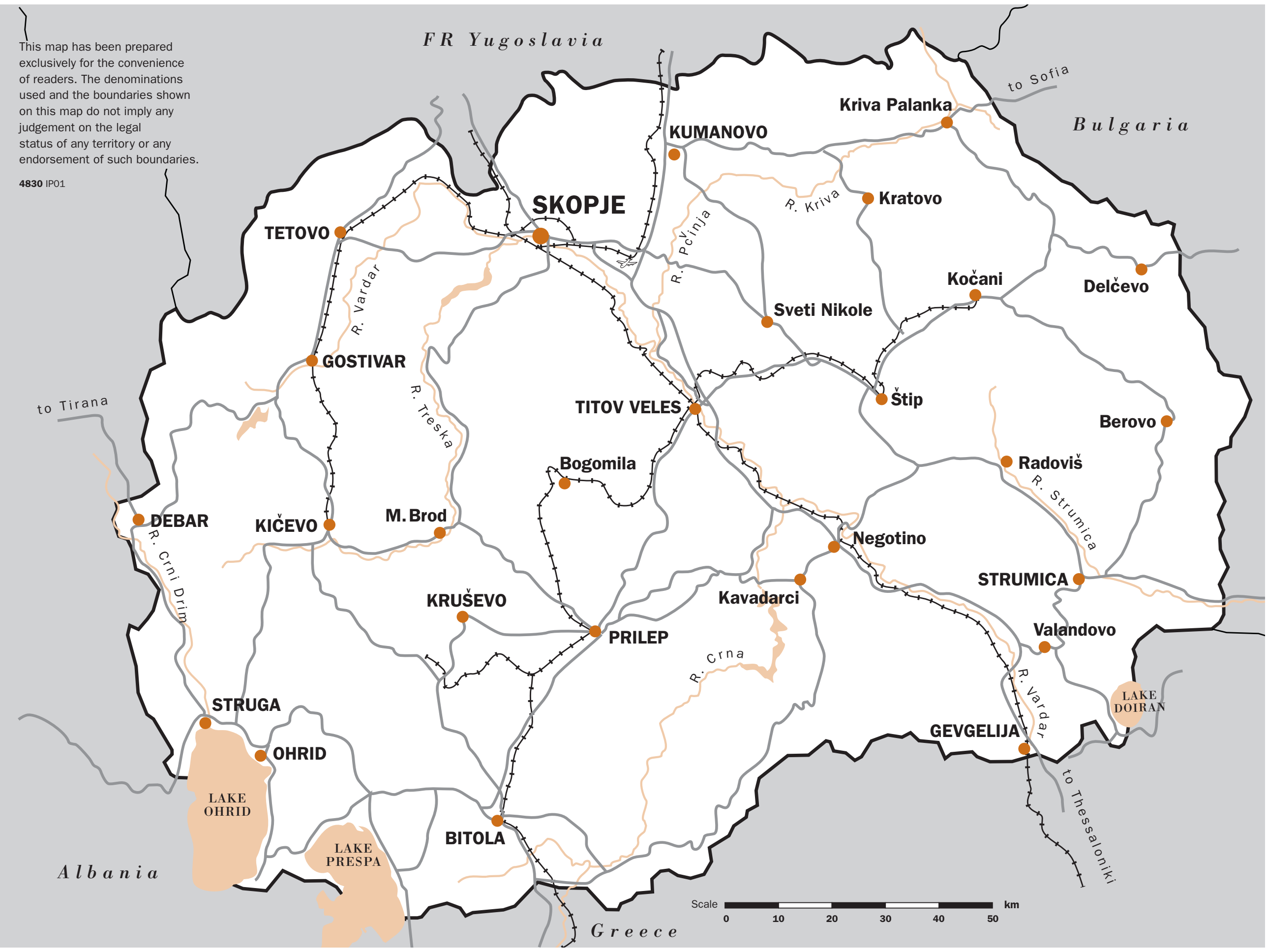
Alongside the IPRSP drawn up as the foundation for the PRGF programme, the government has drawn up a three-year economic programme for 2000-03 which aims to address many of these challenges. Its key medium-term objective is to reduce poverty, as about one-fifth of the population is living below the poverty line. The government considers rapid and sustained growth as the main basis for poverty reduction, and has geared its programme of structural reforms to generating high growth within a stable financial environment. The main elements are:

- reducing the excessive direct tax burden, reforming public administration and rationalising expenditures;
- addressing the problems of key loss-making enterprises through sale or closure and improving the business enabling environment for private sector firms; and
- strengthening the regulatory framework of the banking system and improving the quality of bank intermediation.

Monetary policy will continue to support the exchange rate anchor and complement fiscal policy in maintaining financial stability and promoting structural change.

A crucial factor for the realisation of these aims will be stronger political stability. The past year has been marked by political polarisation and a weakening of the position of the ruling coalition. Local elections held in September did not go well for the government parties, which suffered heavy losses in the mainly Slav areas including Skopje. In the last quarter of 2000 the Liberal Party entered the ruling coalition, substituting for the departing Democratic Alternative (DA). However, these events did not dislodge the present coalition. Instead, five ministers were replaced and a government crisis was averted.

In balance, the new IMF and World Bank programmes will help to guarantee transition progress and greater investor confidence. Another major positive factor is the greatly improved regional outlook following the democratic revolution in neighbouring FR Yugoslavia.


This map has been prepared exclusively for the convenience of readers. The denominations used and the boundaries shown on this map do not imply any judgement on the legal status of any territory or any endorsement of such boundaries.
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Economic summary

The Macedonian economy has made a strong and sustained recovery from the Kosovo crisis in 1999. Preliminary estimates for 2000 suggest that real GDP growth exceeded 5 per cent, the highest rate of growth in the country since the start of transition. Growth prospects for the future have been bolstered in recent months by a Stabilisation and Association agreement with the EU and new programmes with the IMF and the World Bank.

GDP growth

The economy grew strongly in 2000 at an estimated rate of 5.1 per cent, thereby continuing the recovery that became evident soon after the end of NATO bombing in Yugoslavia in June 1999. Much of the recovery is concentrated in the western part of the country adjacent to Kosovo, reflecting large increases in construction, trade and services. However, registered unemployment remains stubbornly high at around 30 per cent of the labour force and one-fifth of the population is estimated to live below the poverty line. The government's new Interim Poverty Reduction Strategy Programme (IPRSP) is designed to address these problems. The 2001 budget, adopted on 1 February 2001, assumes that real GDP growth in 2001 will be 6 per cent.

Inflation

Inflation rose in 2000 to about 6 per cent by end-year reflecting higher oil prices and the one-off effects of the introduction of VAT in April, but is expected to come down again in 2001 to 2-3 per cent. The 2001 budget assumes a level of 2.2 per cent. The goal of monetary policy is to maintain a low inflation level not exceeding 3-4 per cent per year, using the exchange rate peg (see below) as an anchor against high inflation.

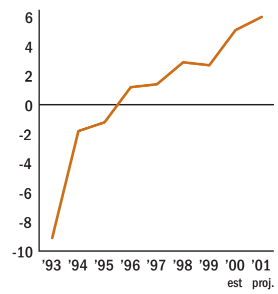
Exchange rate

The denar (MKD) is pegged to the D-mark and thus fell against the US dollar in 2000 averaging MKD 65.9 to the dollar compared with MKD 56.9 in 1999. In a letter of intent to the IMF on 15 November the government stated that the central bank (the NBRM) would continue its policy of pegging the denar to the D-mark. It added that the NBRM is considering moving to a more flexible exchange rate regime once enterprise and banking sector reform have been implemented.

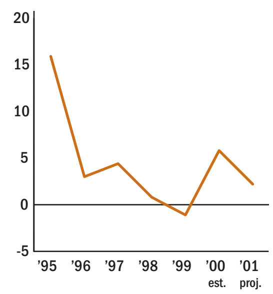
Current account

The current account deficit, which had improved in 1999, has started to widen again as pent-up import demand was released. The low domestic savings rate and difficulties in accessing new markets suggest that current account difficulties are likely to be persistent over the short-term, thus highlighting the importance of attracting greater flows of FDI. However, over 2001 the deficit may narrow as exports to the EU and FR Yugoslavia increase.

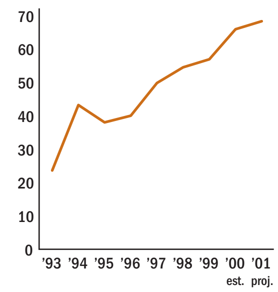
GDP
% change



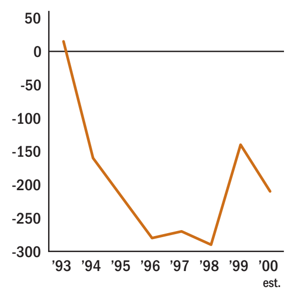
Consumer prices
Annual average, % change



Exchange rate
Annual average, denars per US$

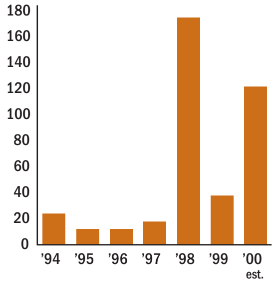


Current account
US$ millions

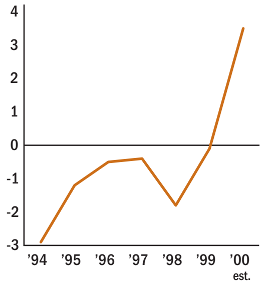


Source: Ministry of Finance, January 2001

Total FDI
US$ millions, cash receipts, net



General government balance
% of GDP



Source: Ministry of Finance, January 2001

Foreign direct investment and privatisation

FDI rose sharply in 2000 to an estimated US$ 121 million, from only US$ 38 million in 1999, thanks mainly to several large privatisations. The government gained a windfall when the telecoms monopoly was sold to Matav (Hungary) in January 2001 for € 343.3 million, which will be used to reduce foreign and domestic debt, finance infrastructure projects, settle arrears to pensioners and owners of frozen foreign-currency accounts, and invest abroad to earn future income.

Government balance

Fiscal performance in 2000 was strong, in part due to the smooth introduction of VAT, and the government recorded a surplus of over 3 per cent of GDP for the year as a whole. The government aims at a balanced budget over the longer term, with a deficit not exceeding 1 per cent of GDP. Economic growth and tighter revenue collection should enable this to be broadly achieved in 2001-02. Under the 2001 budget, total revenues are projected at MKD 53 billion and expenditures at MKD 61 billion. The resulting deficit will be financed by external credits and donations. To boost industry and employment, company and personal income taxes and VAT rates are reduced in the new budget. The budget also envisages US$ 180 million of external debt service, a decrease of expenditures on salaries in the state administration and more funds for development and implementation of infrastructure and public projects. Personnel in the state administration is to be reduced by some 3,500 jobs in line with IMF and World Bank funding requirements, through early retirement and voluntary redundancy.

EU agreements

To counteract the negative effects of the Kosovo crisis, additional assistance to that already promised by the EU is being made under the framework of the Stability Pact. The previous Trade and Co-operation Agreement with the EU has been upgraded to a Stabilisation and Association Agreement, which was agreed in late 2000 and will be signed on 10 April 2001. This agreement is meant to result in mutual free trade in 10 years, and free trade in industrial products in the short-term. In 2000 the EU agreed to provide € 80 million for support of balance of payments, of which € 30 million is grant funding. In January 2001 the first € 30 million instalment was disbursed. EU funding is also being provided for reform of the justice and interior sectors, approximation of Macedonian legislation with EU laws, institutional stabilisation and social development.

IMF and World Bank agreements

The IMF has enjoyed a strong relationship with successive Macedonian governments during the transition, and was in the middle of its second three-year ESAF programme when the Kosovo war erupted. Because of the macroeconomic difficulties associated with the war, the programme was suspended. Article 4 consultations were completed in January 2000 and the IMF Board approved a new three-year programme in late 2000. The programme is a mixture of an Extended Fund Facility (EFF) of US$ 31 million and a Poverty Reduction and Growth Facility (PRGF) of US$ 13 million. The PRGF was conditional upon the World Bank's approval of the IPRSP, which was approved on 14 December.

At the same time, the World Bank also approved a new Financial and Enterprise Sector Adjustment Loan (FESAL-II) programme for US$ 50.3 million, intended to support enterprise reform, encouraging the private sector and job creation. Along with the reductions in public administration jobs, the main condition for both IMF and World Bank funding is the sale or liquidation of large loss-making enterprises in three phases by March 2002 (see *Investment climate: Privatisation* below). Under the new programme, 40 loss-making enterprises are targeted for privatisation or liquidation over the next two years.

Following a Country Assistance Strategy (CAS) issued in 1998, in June 2000 the World Bank issued a progress report reviewing its implementation, and recommended that in view of its economic progress the country should graduate from access to concessional IDA funds. From 1 July 2001 it will only have access to IBRD financing and a new CAS is being prepared for presentation to the Executive Board of the World Bank in mid-2001.

Selected economic indicators

	1993	1994	1995	1996	1997	1998	1999	2000 est.	2001 proj.
GDP (% change)	-9.1	-1.8	-1.2	1.2	1.4	2.9	2.7	5.1	6.0
Consumer prices (annual average % change)	349.8	121.8	15.9	3.0	4.4	0.8	-1.1	5.8	2.2
Current account (in US$ millions)	15	-160	-220	-280	-270	-290	-140	-210	na
General government balance (% of GDP)	-13.4	-2.9	-1.2	-0.5	-0.4	-1.8	-0.1	3.5	na
Trade balance (in US$ millions)	43	-186	-221	-317	-386	-419	-408.0	-601.0	na
Total FDI (in US$ millions, cash receipts, net)	0	24	12	12	18	175	38.1	121.8	na
External debt stock (US$ millions)	818	844	1,062	1,118	1,131	1,398.6	1,438.5	1,427.6	na
Unemployment (% of labour force)*	28.3	31.4	37.7	31.9	36.0	34.5	32.4	32.1	na
Exchange rate, annual average, denars per US$	23.6	43.2	38.0	40.0	49.8	54.5	56.9	65.9	68.3
Gross reserves, excluding gold (end-year, US$ millions)	105	165	257	240	256	304	427.7	na	na

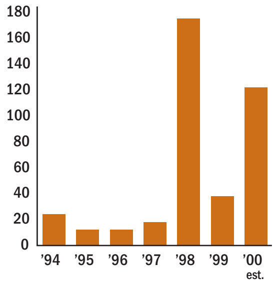
** The figures provided up to 1995 refer to officially registered unemployment. From 1996, they are based on a labour force survey.*
Source: Ministry of Finance, January 2001

Investment climate

On the back of regional stability, FDI is picking up. The government is working to amend the relevant legislation to create a more attractive investment climate. Most investment comes from privatisation, which has accelerated in the past year. Conclusion of the Stabilisation and Association Agreement with the EU will allow for largely duty-free trade with EU member states.

Foreign direct investment

Total FDI
US$ millions, cash receipts, net



Source: Ministry of Finance, January 2001

In March 1999 the government adopted a programme for stimulating investment, with special emphasis on attracting foreign direct investment (FDI). While foreign investors remain cautious, their activities are increasing. After a surge in 1998, FDI fell back in 1999 to around US$ 30 million. The Kosovo crisis deterred investors, but the renewed stability in the region has led to increased interest. Total net FDI in 2000 is estimated at US$ 121.8 million. According to EBRD data, cumulative FDI from 1994 to 2000 totals some US$ 368 million.

Most FDI comes through privatisation receipts and post-privatisation transactions at the Macedonian Stock Exchange. The largest foreign investments in 2000 were the acquisition (agreed in late 1999) of a 65 per cent stake in Stopanska banka by the National Bank of Greece (see *Financial sector* below) and (at the very end of the year) the sale of 51 per cent of the telecoms monopoly Makedonski Telekomunikacii (Maktel, or MT) to Matav (Hungary) (see *Major sectors of the economy: Telecommunications* below).

The leading source of foreign investment is Greece, followed by Liechtenstein and Cyprus.

More than 90 per cent of FDI has been invested in manufacturing (ferrous metallurgy, cement, crude oil processing, food and beverages, and textiles). In the year 2000 significant FDI was attracted in the insurance and banking sectors.

Investment policy and incentives

Foreign investment is governed by the Law on Trading Companies, which allows for companies to be established by domestic and foreign natural and legal persons on equal terms. Incentives for foreign investors include customs duty exemptions on imports of equipment and other assets to be used for capital contributions, and profit tax relief for the first three years (see below). Another incentive is the standard 15 per cent corporate tax rate.

The government recently adopted a new law on free-trade zones and the first zone, Skopje Free Economic Zone (SFEZ, also known as the Bunardzik free trade zone), is under construction. The government of Taiwan, which has been a generous investor in a number of areas including education, healthcare, roads and IT, is providing financial support for the FEZ initiative. Incentives include a number of tax exemptions on customs duties, profit tax (for 10 years), property tax (for 10 years), etc.

Top 10 foreign investments through privatisation and post-privatisation

Name	Country	Sector	Investment	Size of investment, US$m (excluding commitments)
National Bank	Greece	Banking	Stopanska Banka	46.4
Balkanbrew Holding	Greece	Food processing	Skopje Brewery	34.0
Hellenic Petroleum	Greece	Petrochemicals	OKTA refinery	32.0
Titan, Holderbank	Greece, Switzerland	Construction	Usje cement factory	30.0
Balkan Steel	Liechtenstein	Metallurgy	Ladna Valalnica	21.0
QBE Insurance	UK	Insurance	ADOR Makedonija	14.8
Duferco	Switzerland	Metallurgy	Makstil	11.5
East West Trade	Austria	Retail trade	Centro	11.0
KUPP.BALL und Transthandel	Germany	Metallurgy	FZC Kumanovo	3.35
SCMM	France	Metallurgy	Feni-Kavadarci	2.25

Source: Macedonian Privatisation Agency

Legal information for investors in brief

Foreigners may establish general partnerships, limited partnerships, limited liability companies (minimum capital equal to DEM 10,000), joint stock companies (minimum capital equal to DEM 20,000 for companies incorporated simultaneously and DEM 50,000 for companies incorporated successively) or limited partnerships by shares. They may also open representative offices or branches.

The legal framework includes a Law on Public Procurement (1998), regulating all procedures of public procurement and aiming to ensure transparency and equal access for all interested parties. Dispute resolution is governed by the Constitution, the Litigation Procedure Law, and a law on settlement of disputes. The country is a signatory to the main international conventions on commercial arbitration, and ratified international agreements take precedence over domestic legislation.

The **taxation system** has been amended to make it more attractive to foreign investors. **Corporate income tax** is charged at a rate of 15 per cent, and taxable income is reduced by the amount of profit reinvested in fixed assets, new investments, and the purchase of stocks and shares up to the amount invested. Investments in designated underdeveloped regions qualify for relief of up to 100 per cent of taxable income. The tax base of companies with foreign shareholdings of at least 20 per cent is reduced by the proportion of the foreign investment for the first three years after the investment is made. There is no tax on transferred profit.

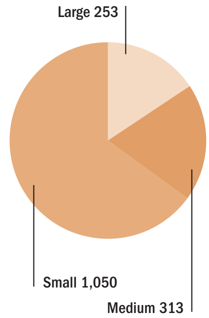
Based on the average monthly salary, **personal income tax** is charged at rates ranging from 15 per cent to 18 per cent. These rates were introduced from 1 January 2001, in place of rates ranging from 23 to 35 per cent. **Payroll contributions** payable by the employer include health insurance (8.6 per cent), pension fund (20 per cent) and employment (1.5 per cent). Under the law on **property tax**, land and buildings are taxed on their market value at an annual rate of 0.10 per cent. **VAT** came into force from 1 April 2000, replacing the existing sales tax, and is charged at a basic rate of 19 per cent, with a reduced rate of 5 per cent on certain goods and services (e.g. food and agricultural products, books and newspapers, fuel and energy supplies, and pharmaceuticals). The list of items qualifying for the 5 per cent rate was increased in the 2001 budget. Various goods and services are exempt from VAT (or zero-rated), including exports and services related to exports and imports. **Excise duties** are charged on certain goods including tobacco products, liquor, fuel and natural gas, coffee, cars and luxury goods, at rates ranging from 5 to 55 per cent.

The government is also undertaking a number of measures to address concerns raised by foreign investors, in view of inconsistencies in the legislation and cumbersome bureaucracy. These measures include plans to set up a one-stop shop for registration of foreign investors, amendments to strengthen legislation on mortgages, bankruptcy and property rights, and possible increased tax exemptions. The government introduced two new competition laws at the end of 1999, a law on restricted competition and an anti-monopoly law. This is a new area for the judiciary in the country and it remains to be seen whether enforcement will be effective. Legislation on land ownership for foreign investors and on the right to repatriate profits also require greater clarity.

Privatisation

The privatisation programme continues to move forward. By 31 December 2000, 1,616 companies had been privatised and a further 126 enterprises were in the process. Significant progress has been made in the agricultural sector, where 403 companies were privatised by the end of 2000 (compared to 323 at the end of 1998) and a further 30 were in the process. Meanwhile, a programme to sell or liquidate 12 large, loss-making enterprises, launched in 1998, accelerated in 2000 after encountering significant delays. The success of

Number of privatised companies by size



Source: Macedonian Privatisation Agency

Privatisation progress at 31 December 2000

Sector	No of companies privatised	No of companies in process
Manufacturing	481	37
Agriculture	403	30
Construction	118	9
Trade	339	27
Transport and traffic	52	3
Finance and services	111	12
Craft	54	2
Catering and tourism	58	6
Total	**1,616**	**126**

Source: Macedonian Privatisation Agency this programme was a pre-condition for World Bank funding. However, the government had been reluctant to add to the already very high levels of unemployment and the Kosovo crisis in 1999 appears to have deterred potential investors. Nevertheless, by the end of 2000, 11 of these enterprises had either found private investors (such as Fenimak), been sold to workers or liquidated, with the remaining enterprise scheduled for sale or closure by the end of March 2001.

A **new list of 40 loss-making state-owned companies** has been drawn up, with a target of sale or liquidation by mid-2002. Under the terms of the new FESAL-II loan from the World Bank, chromium producer Jugochrom and three other companies are to be sold or liquidated in the first half of 2001, from among the Zletovo smeltery, the Zletovo battery producer or the Zletovo mine, Sasa mine (lead and zinc), Gotex, Porcelanka (ceramics), Godel (leather and fur) and FAS Octomvri 11 (bus producer). To support the privatisation of loss-making companies, the Privatisation Agency has cut selling prices substantially, in some cases by up to 95 per cent. It has put 74 per cent of Jugochrom on offer for DEM 2 million, compared with an original valuation of DEM 51.2 million. Jugochrom is heavily indebted, mainly to the state electricity utility, Elektropanstvo na Makedonija (ESM).

Loss-making enterprises manage to stay in business by defaulting on payments to employees, other firms (thus passing on the burden of debt) and the government, and continue to receive loans from banks. In September ESM for the first time cut off electricity to some of the worst offenders.

Large-scale enterprise privatisation is moving forward, most notably with the recent sale of the telecommunications monopoly to Matav of Hungary (see *Major sectors of the economy: Telecommunications* on page 16). On the new list of 40 companies to be sold or liquidated by the end of 2002, the largest and most attractive firm is the electricity utility, ESM (see *Major sectors of the economy: Energy* on page 14).

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Markets and trade

The Law on Customs Duties was amended in February 2001 to lower duties on over 4,000 products including raw materials, computers and construction materials. The biggest reduction, of some 50 per cent, is for pharmaceutical products. The measure aims to reduce the grey economy and develop the private sector.

Trade with the EU is increasing steadily, and is also expected to grow as a result of the EU's extension of trade preferences for the western Balkans, making 95 per cent of most goods free of customs duty. In late 2000, the country completed negotiations with the EU on a Stabilisation and Association Agreement (SAA), upgrading the previous Trade and Cooperation Agreement. The SAA is designed to result in mutual free trade in 10 years, and free trade in industrial products in the short term. The negotiations focused on

Top 10 trading partners, January-September 2000, US$m

Country	Export	%	Import	%
Germany	192.6	19.5	187.3	12.1
FR Yugoslavia	236.2	23.9	142.0	9.2
Greece	61.2	6.2	140.3	9.1
USA	135.4	13.7	56.0	3.6
Slovenia	19.5	2.0	105.1	6.8
Italy	70.2	7.1	83.6	5.4
Ukraine	0.3	0.0	169.1	10.9
Bulgaria	20.0	2.0	70.8	4.6
Croatia	32.6	3.3	44.7	2.9
Russia	7.5	0.8	130.5	8.4
Total	**989.0**	**100.0**	**1,550.9**	**100.0**

Structure of trade by regions, January-September 2000, %

Region	Export	Import
Developed countries	62.3	47.7
EU	43.5	37.8
EFTA	3.2	1.5
Other	15.6	8.4
Developing countries	2.2	4.9
Central & eastern Europe and FSU	4.2	28.3
Countries of former Yugoslavia	31.0	19.1
Other countries	0.3	0.1

Source: Macedonian Statistical Bureau

regional economic and financial cooperation and adaptation of legislation to EU norms. The World Bank is helping the country reach EU customs standards as part of its Trade and Transport Facilitation in Southeastern Europe project (see *Major sectors of the economy: Transport* below). The country has observer status with the WTO and opened formal accession negotiations in July 2000.

Exports to the countries of former Yugoslavia rose strongly in 2000, although imports fell slightly. FR Yugoslavia has traditionally been a major trading partner, and the figures reflect the republic's return to the Yugoslav market following the political change in Belgrade. Trade between the two countries is expected to grow, and the republic is likely to win new construction contracts and to re-establish its business links with Serbia.

In January a free trade agreement was signed with Ukraine, which will contribute to reducing the trade deficit by making exports cheaper. Free trade agreements are also in place with FR Yugoslavia, Bulgaria, Turkey and EFTA. Negotiations for a similar agreement with Albania are expected to be concluded during the first half of 2001.

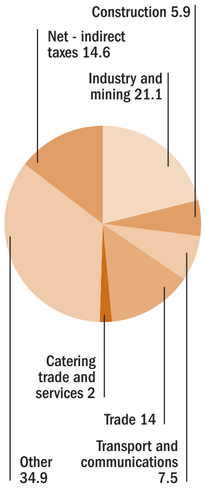
Pension reform is progressing. The government has enacted a number of reforms, effective from September 2000, to the pay-as-you-go pension system. They include a gradual increase in the retirement age for men from 63 to 65 years of age, and for women from 60 to 63, and indexing pensions to both the CPI and wages (as opposed to the former system of wages only). The legal framework for a fully funded mandatory second pillar is now in place and the system will be introduced in the medium term.

Major sectors of the economy

Major foreign investments have been made through the privatisation of the telecoms company and of the country's only oil refinery. Opportunities exist in the forthcoming energy sector privatisation, in mining and metallurgy, and in the growing services sectors.

Industrial output grew by 10.6 per cent year on year in the first six months of 2000, but gradually slowed to reach only 5.3 per cent in the first nine months. In the same period output increased in metallurgy, chemicals and construction materials in particular. Agricultural output was adversely affected by drought in 2000. Services continued to grow thanks to demand in transport and telecommunications generated by international forces stationed in Kosovo, who often visit the country when on leave. There is also a NATO force still present in the republic, which accounts in part for an increase in retail trade. Retail trade was also boosted in March 2000 when consumer spending rose in anticipation of price rises before the introduction of VAT in April.

Origins of GDP by sector
2000, per cent



Source: Macedonian Statistical Bureau

Structure of industrial production, as at December 2000, %

Electricity production	17.4
Coal production	2.1
Iron and steel industry	4.3
Production of non-ferrous metals ores	1.8
Non-ferrous metal production	3.0
Metallurgy	3.2
Electrical goods	5.1
Base chemical products	5.5
Chemical products processing	6.1
Construction materials	5.1
Textiles, yarns and cloth	2.3
Final textile products	6.0
Food processing	11.9
Tobacco production and processing	6.8
Beverage production	5.9
Other	13.5

Source: National Bank

Agriculture and agribusiness

The agricultural sector is well developed and currently contributes around 9 per cent of GDP. The moderate climate, sunny valleys, vast vineyards, and a modern irrigation system create ideal conditions for growing high-value early-season fruits (including cherries, peaches, apricots and grapes) and vegetables. Another important crop is tobacco (see below). In former Yugoslavia, the country was a leading supplier of agricultural production. Wheat, barley, corn and other traditional crops are also grown, and the livestock sector is significant. A long-term development plan aims to increase both fruit tree plantations and land planted with crops by 50 per cent each.

While harvests were good in 1999, in 2000 agriculture was hit by drought, which reduced the wheat harvest by 16 per cent, to 320,000 tonnes, which will necessitate imports to meet annual consumption. The maize crop also suffered a large drop. In all, agricultural output is estimated to have fallen by 1 per cent. However, the grape harvest recorded a 16.3 per cent rise year-on-year.

Privatisation of the agricultural sector is largely complete, with 403 enterprises sold by the end of 2000 and 30 more in the process. Three large agricultural kombinats were privatised in late 1998 (representing 15 per cent of the total), each split into a number of smaller companies. Most privatisation has been through sales to existing managers and farmers.

Various international agencies have provided support to the agriculture sector. The EU is assisting the Ministry of Agriculture in policy and strategy development towards the open market, and in bringing animal and plant health controls to EU standards. The EU also helped to draft a new law on agricultural land, which is now in force. An agricultural development agency has been established, co-funded by the World Bank's Private Farmers' Support Project and the government, to provide professional assistance to farmers to help them improve the quality and quantity of agricultural production. Based in Bitola, it has units countrywide providing financial assistance, training and information and cooperation systems. In December 2000 the International Fund for Agricultural Development announced a grant of US$ 8 million for agricultural sector development, specifically to improve living standards for the rural population and to fund small agribusiness enterprises.

Agricultural land ownership

Most agricultural land is privately owned. Although much of the land is distributed among small family farms, the Law on Agricultural Land passed in 1999 abolishes the former restrictions on land ownership and gives impetus to the enlargement of existing farms. The legislation provides rules for the use of state land under concession terms or long-term rental arrangements. There are 40-year concessions for arable land, and 20-year concessions for the use of land for breeding livestock. Land will be offered for rent at public auctions, where both domestic and foreign entities may bid for it.

Agribusiness as a whole, including agriculture and processing, accounts for almost 19 per cent of GDP. Tobacco is an important sub-sector, accounting for over 6 per cent of the gross industrial product. Food and beverage processing are developed industries, with companies producing canned and bottled fruits and vegetables, and wine and beer for export. Falling wine prices in the principal export markets have led to a fall in the revenue from wine sales.

Brewing

The country produces about 1 million hectolitres of beer each year, mainly for the domestic market.

In the second half of 1999 the government made a determined effort to sell the Bitola Brewery, one of the loss-making enterprises on the government's list of companies that must be sold or close as a pre-condition to World Bank lending. In January 2000, the government accepted the offer of Kenri GmbH (Switzerland) to buy the brewery for DEM 100,000 (US$ 51, 000) and pay the brewery's current debt of DEM 4.5 million (US$ 2.4 million). Kenri also promised to retain the workforce and to invest DEM 16.2 million over three years. Kenri is installing new German technology and aims to produce Turkish Efes Pilsen and American Budweiser brands under licence for export to the neighbouring countries and to the US.

Skopje Brewery has benefited from the acquisition of a majority stake by Heineken (Netherlands). The investment was made through Brewinvest, a joint venture in cooperation with Hellenic Bottling (Greece). The investors paid US$ 35 million for a 51 per cent share in the brewery, which makes the country's leading brands of beer (Star Lisec and Skopsco, holding over two-thirds of the market), and also bottles Coca-Cola, Fanta and Sprite. The investors are installing new machinery to modernise production and improve beer quality.

Wine

Wine grapes are grown on over 30,000 hectares of land, producing about 250,000 tonnes of grapes annually, the bulk of which are processed into 1.3-1.4 million hectolitres of wine. Exports to the EU total some 75,000 hectolitres each year. Exports in 1999 totalled 67.7 million litres, bringing revenue of US$ 25 million. However, the sector needs substantial investment if it is to achieve its full potential. Challenges for the wine producers include increasing the volume of bottled wine and stimulating grape production. Achieving brand recognition is also a priority. A long-term development plan aims at major expansion of viticulture, with a 40 per cent rise in the number of vineyards.

The Povardarie winery at Negatino has modern facilities and produces from 100-130 million litres of wine a year, exporting to destinations including western Europe.

Tobacco

The hilly terrain and dry climate create excellent conditions for growing high quality tobacco in all regions of the republic. The country produces from 25,000 to 35,000 tonnes of tobacco each year. Tobacco is the most important export commodity in the agribusiness sector. Before independence it accounted for 70 per cent of all tobacco production in former Yugoslavia. It now comprises around 5 per cent of the country's total exports. Harvests have risen in the past few years, partly as the result of improved procedures for paying for the tobacco, as well as the presence of foreign investors.

There are 24 fermentation plants and three cigarette-making factories, producing up to 20,000 tonnes of cigarettes each year. High quality raw materials have attracted the interest of several multinational tobacco companies, who already purchase most of the country's production. The sector has strong export potential, especially for Virginia-blend cigarettes, for which the country has excellent climatic conditions. One of the largest tobacco factories, Tutunski Kombinat in Prilep, won a prize from the Euromarket trade association in December 2000 for increasing its production in 2000 by 70 per cent compared with 1998 and by 10 per cent year on year, exceeding its output plan for 2000 by 25 per cent.

In 1999 **Tobacna Ljubljana** (Slovenia, 58.8 per cent owned by Germany's Reemstma) bought an 80 per cent stake in the Tutunski Kombinat in Skopje, one of the country's largest tobacco plants, for DEM 8 million. Within a year Tobacna had achieved its aim of increasing the company's domestic market share from 20 to 50 per cent, thanks to successful efforts to bring production up to European standards. Tobacna is investing over DEM 15 million up to 2004, and plans to penetrate the Bulgarian and Albanian markets as well.

Other foreign companies involved in the tobacco sector include Michailidis (Greece), which owns 50 per cent of the Jugotutun tobacco processing plant in Kochani. The buyer purchased the shares owned by the employees at their market price, promised to solve the company's financing problems and also to stimulate the production of Virginia-blend tobacco. The Kumanovo Tobacco Factory, valued at US$ 17.5 million, is seeking a strategic investor. In June 2000 it launched three new brands of cigarette.

Chemicals and pharmaceuticals

The large chemical industry accounts for about 10 per cent of industrial output. It produces basic chemicals, acrylic fibres, polyvinyl chloride, detergents, fertilisers, polyurethane foams and fibres. There are also a number of successful pharmaceutical and cosmetics firms.

Challenges for the sector include dependence on import of a high proportion of raw materials and semi-finished products, and also lack of investment for modernisation to meet quality standards required for export. However, foreign investment has been increasing, especially in the pharmaceuticals sector.

ICN Corporation (US) has a joint venture with OHIS, a Macedonian drug producer, and has invested around US$ 15 million. The new company, ICN Makedonija, produces and distributes a wide range of drugs. Two German firms, Alpha Plan and Saxonia Medical, also have a joint venture with OHIS and are investing DEM 10.5 million in a new pharmaceutical factory to make products for the German export market. Other market leaders include former Yugoslav firms such as Lek and Krka (both Slovenia) and Pliva (Croatia). Lek has invested US$ 14.5 million in a new production plant to make the most advanced drugs using state of the art technology and aims to access the over-the-counter drugs markets in Albania, Bulgaria and Greece.

In July 1999 major pharmaceuticals firm **Alkaloid AD Skopje** concluded a transaction with the EBRD and the IFC for loans to develop its products to meet EU certification standards. Alkaloid is a Skopje-based, 100 per cent locally owned private company manufacturing pharmaceuticals, chemicals, cosmetics, coatings and food products. The EBRD/IFC project will help the company to become integrated into the international economy, and will also promote private sector development. The credits total € 17.4 million (approximately US$ 17.7 million), which will be used to finance upgrading and modernisation of pharmaceutical production facilities. Total project cost is estimated at about US$ 36 million.
Founded in 1936 with 15 workers, Alkaloid was the first plant in the Balkan region to produce pharmaceutical products. Through subsequent mergers and acquisitions it increased its scope of activity to include the production of a variety of finished drugs, medicinal herbs, cosmetics and fine chemicals. Alkaloid was privatised in 1995 and has become one of the most successful companies in the country and a leader in the domestic pharmaceutical sector.

Energy

State electricity utility Elektropanstvo na Makedonija (ESM) is responsible for the generation, transmission and distribution of electricity. It runs three thermo-electric stations with installed capacity of 1,010 MW powered by lignite and oil, six hydro-power stations with installed capacity of 390 MW and nine with installed capacity of 34 MW, as well as lignite coal mines. The main thermal plant at Bitola supplies about 70 per cent of the country's production and is in good condition.

ESM has gradually been undergoing preparation for privatisation and is likely to be sold as a vertically integrated company. Although the sale is not likely to take place until 2002 or later, Enron (US) and RWE (Germany) have already expressed interest and are holding talks with the government. With a view to entering Europe, the government has been working to restructure, liberalise and open the electricity market to competition. It has not yet decided how much of ESM to sell off, and whether or not it will retain a golden share. It is thought that a regulatory body will be established to mediate between the interests of ESM's future owners, the government and consumers. It is also possible that ESM shares may be floated on the Macedonian stock exchange in the near future, and also on international markets. ESM employs about 7,000 people and has an estimated value of almost US$ 3 billion.

The government has drawn up an investment programme for ESM worth a total of US$ 276 million for projects to be carried out over the next few years, including a new gas-fired thermal energy plant near Skopje, a new hydropower plant near Debar, renovation of existing hydropower plants and new transmission links with neighbouring countries. A major World Bank initiative, the Power System Improvement Project, started in 1998 and will run until 2005. Worth a total of DEM 61.5 million, it aims to rehabilitate the hydropower system. The main elements of the project are the renovation of the six largest plants at a cost of US$ 31.6 million, establishment of an energy management system for US$ 8.7 million, and rehabilitation of the distribution system to reduce losses, at a cost of US$ 4.3 million.

In late 2000 ESM was owed some DEM 250 million in unpaid bills. In September for the first time it cut off electricity to some of the loss-making large enterprises that have consistently failed to pay their energy bills.

Transport

The country has an adequate network of roads totalling over 9,400 kilometres, of which half are well-maintained paved highways. Links to the neighbouring countries are in need of renovation. The country's strategic location as a Balkans crossroads has attracted international finance to upgrade its motorway network. A number of major projects are in progress, financed by IFIs including the EU, the EIB and the World Bank.

Two key Pan-European Transport Corridors cross the country and intersect at Skopje, forming part of the Trans-European Network identified by the EU for development. These are Corridor VIII (the E-65 east-west road, from Durres on the Albanian coast via Tirana, Skopje and Sofia to Varna on the Bulgarian Black Sea coast), and Corridor X (the E-75 south-east-north road from Thessaloniki on the Greek coast via Skopje, Belgrade and Zagreb to Munich).

The five-kilometre stretch of Corridor X from Gevgelija to the border with Greece has been upgraded at a cost of DEM 18 million. Through an EIB Financial Protocol the EU has contributed EUR 70 million to upgrading of the Skopje-Tetovo stretch of Corridor VIII (now completed) and the highway from Gratsko to Demir Kapija. The World Bank (under its Transport Sector Project), Phare and the country itself are covering the rest of the financing, a total of EUR 141.5 million. The EIB plans to finance the link from Demir Kapija to Gevgelija, and also a ring road for Skopje. The EBRD is also helping to finance the Skopje bypass project as well as a stretch of the E-75 route. Other donors include Greece and Taiwan (ROC), who are jointly contributing over € 120 million.

The World Bank is funding a project for **Trade and Transport Facilitation in Southeast Europe**, which involves modernisation of customs administration, upgrading of information systems, improvements to border crossing infrastructure and equipment and technical assistance for trade facilitation. This regional programme involves Albania, Bosnia and Herzegovina, Bulgaria, Croatia, and FYR Macedonia. An investment of up to US$ 140 million is planned for the period to 2003. The main sources of financing will be the World Bank (US$ 38 million), its soft-loan arm the International Development Agency (US$ 30 million), the US government (US$ 9 million), and the EU (US$ 50 million), with participating countries providing US$ 18 million. This programme will represent the first regionally linked project in support of the Stability Pact.

Railways

The country has a railway network of some 700 kilometres. Until recently, the country lacked an east-west railway route. Construction of a 55-kilometre railway route from near Kumanovo on the FR Yugoslavia border to the Bulgarian border began in 1995 and is near completion, at a total cost of US$ 335 million. The route is part of a new east-west line connecting Varna on the Bulgarian Black Sea coast with Durres on the Albanian Adriatic coast.

The World Bank's ongoing Transport Sector Project aims to improve the efficiency of the railway system as well as the roads. The railway element includes supply of equipment, technical assistance and training for Macedonian Railways and will support its organisational restructuring and improve its financial viability.

Air transport

In view of rising traffic Skopje's Petrovec international airport is to undergo expansion, for which the government has sought financing from the EBRD. The project will involve an extension of the airport terminal and development of new facilities at an estimated cost of € 40-50 million. A US consultancy group has been engaged to manage the project. The airport has already undergone some renovation and expansion, with EBRD financing for a runway and equipment upgrading provided in 1995.

Skopje airport is served by six airlines with direct flights to and from various European cities and connections via Ljubljana (Slovenia) and Zagreb (Croatia). A second airport serves Lake Ohrid. Both are operated by a public company, which has a consistenly high operational rating. Two new civil airports are to be constructed at Bitola and Strumica under a long-term development plan.

The country has two airlines, Macedonian Air Transport (MAT), the former Yugoslavia's flag carrier, and Avioimpex. In November 2000 the two companies started merger talks, with a view to becoming more competitive with international airlines. The talks are expected to be completed by mid-2001. Avioimpex has six aeroplanes and transported 312,000 passengers in the first 10 months of 2000. MAT uses four leased planes and transported 268,000 passengers in the same period.

Telecommunications

The government announced in April 2000 that it would sell between 51 per cent and 66 per cent of the state-owned Makedonski Telekomunikacii (MT, also known as MakTel or MakTelekom) to a strategic investor, building on the pre-privatisation programme of the previous government. The sale had been delayed by the Kosovo crisis, but took place in January 2001. Six international companies expressed an interest in bidding, of whom by November 2000 three had been singled out as favourites, a consortium led by Matav (Hungary, 60 per cent owned by Deutsche Telekom), OTE (Greece) and Telekom Slovenija (Slovenia). MT was valued at an estimated US$ 1 billion, but the deal for the 51 per cent stake was for US$ 300 million in view of the rate of risk in investing in the country. After strong competition from OTE, the Matav consortium was the winner, buying the 51 per cent stake for € 343.3 million, and pledging to invest € 255.7 million over the next two years.

MT has a monopoly in fixed-line and other telecommunications services. No date for ending this monopoly has been set, but privatisation is expected to pave the way for full liberalisation of telecommunications services and the implementation of regulatory reforms in line with EU and international norms. As MT is the sole provider of GSM services in the country, the Matav consortium also obtained a 51 per cent stake in MobiMak, MT's mobile telephony branch.

In 1998 MT secured pre-privatisation financing from the IFC and ING Bank (Netherlands). Upgrading of the entire telephone system has been in progress for the last few years, guided by an investment plan for the sector up to the end of 2000. The network has been digitalised with switching systems and fibre-optic cables installed in the main towns and cities, and new optical cables laid to create new international links.

In 1995 the EBRD played a crucial role in the country's telecommunications sector through a US$ 42.6 million loan to Makedonija PTT, which was the name of the state enterprise responsible for telecommunications and postal services before they were separated and MT was formed. The loan contributed to the modernisation of the telecommunications network and the restructuring of the sector. Plans for setting up a fully independent regulator are now being developed.

Mobile telephony

In October 1999 the EBRD made a loan of € 18.7 million to MT to develop mobile services in order to meet the recent sharp upturn in demand, and also to double the capacity of the existing network to accommodate 35,000 more subscribers. MT's analogue mobile phone service is called Mobimak and has some 100,000 clients. Coverage is being expanded to areas where telecommunications services are most needed. This financing is contributing to the further liberalisation of the GSM mobile phone network.

A GSM network made and supplied by Ericsson (Sweden) with a capacity of 25,000 subscribers has been in operation since October 1997, with a switching sub-system designed to support an extension of up to 50,000 subscribers.

In February 2001 the government announced plans to launch a tender for a second GSM licence within the next two months. Several companies had already shown interest, including Matav and OTE.

Oil refining

In October 1999 a 54 per cent stake in Okta, the country's only oil refinery, was sold to Hellenic Petroleum (Greece) for US$ 32 million, that pledged to invest US$ 40 million in modernisation over three years. Okta was originally established as the regional refinery for southern Yugoslavia, and has the capacity not only to meet the republic's annual needs of 1.25 million tonnes of refined products, but also to export to Kosovo and adjacent areas. FR Yugoslavia's refining capacity was destroyed during the Kosovo conflict, offering Okta clear potential to raise sales and operate the plant closer to capacity. Okta also has the

Thessaloniki-Skopje oil pipeline

In December 2000 the EBRD agreed to invest US$ 50 million in the Thessaloniki-Skopje oil pipeline being built by Hellenic Petroleum. The pipeline will carry up to 2.5 million tonnes of crude oil per year, reducing transportation costs and securing a long-term supply of oil to the country, where demand is expected to increase from 1.25 million tonnes a year at present to 1.5 million tonnes in 2006. The Okta refinery, to which the oil will be delivered, has strong potential to become a supplier of petroleum products to FR Yugoslavia, western Bulgaria and other neighbouring countries. This modern small gauge pipeline can also be converted to transport refined products.

The EBRD plans to syndicate half of its loan. Initially the credit will be lent to El Pet Balkaniki, Hellenic Petroleum's operating subsidiary for the west Balkans. Hellenic Petroleum is contributing a further US$ 55 million in cooperation with Aegek SA, a Greek construction group. In total, this is the largest single direct investment into the republic from an EU country. In due course the assets and obligations relating to the pipeline will be transferred to a special pipeline operating company to be established jointly by the Macedonian government, which will own 20 per cent, with El Pet Balkaniki taking 80 per cent. It is anticipated that this company will enter into a contract with the Okta refinery, based on an agreed throughput level rather than the capacity available. The company will be exempted from profit taxes for five years.

The pipeline will run from Hellenic Petroleum's EKO refinery and terminal at Thessaloniki to the Okta refinery in Skopje and will replace existing rail transport. The railway route runs along the River Vardar, the main regional river and principal natural route into the country, as well as an important wildlife habitat. The new pipeline is being built at a distance from the river to protect its sensitive ecosystem by ensuring that there is no risk of it being damaged by an oil spill. Instead it will pass through agricultural land agreed to be of limited ecological importance.

Thus the pipeline is a cheaper and more environmentally sound alternative to the current road and rail transportation, and will give the country access to a reliable source of oil, enabling it to produce oil products for the domestic market and for export. The EBRD's investment not only supports privatisation, but will also contribute to the transition process by creating linkages between the oil sector and other related sectors of the economy. As a further boost for transition, the EBRD has engaged in a policy dialogue with the government concerning long-term oil sector liberalisation. The project will also have an impact on regional integration, through commercial and infrastructure links with Greece and exports to neighbouring countries. The pipeline is expected to come on line by the end of 2002.

ability to deliver consistent products and prices to markets hitherto dependent on contraband and irregular supply. Okta is now supported by a major sponsor, Hellenic Petroleum, the largest oil company in Greece, with the most modern refineries in the region representing 50 per cent of Greek refining capacity and supplying 57 per cent of the Greek crude oil market.

Following its take-over of the refinery, Hellenic Petroleum's subsidiary El Pet Balkanike quickly stabilised production and reduced production losses. It has also integrated Okta into Hellenic Petroleum's management, accounting, reporting, supply and distribution systems. Financial performance has improved markedly, exceeding expectations. Once market penetration has increased and production expanded further, annual turnover is forecast to exceed US$ 400 million. Hellenic Petroleum has also committed (in principal) to invest US$ 20 million in a network of petrol stations throughout the country. To reduce crude oil transportation costs to the country, Hellenic Petroleum is to construct a 221-kilometre pipeline from Thessaloniki in Greece to Skopje at a cost of US$ 105 million, including EBRD financing of US$ 50 million (see *Case study* page 17).

Hellenic Petroleum is the single largest investor in the country. These investments are part of Hellenic Petroleum's strategy to expand into neighbouring countries. Other activities include a 75 per cent equity interest in Global SA, an Albanian wholesale company, and a plan to construct up to 24 retail petrol stations over the next five years, membership in a consortium that plans to construct an oil terminal at Durres on the Albanian coast, membership in the consortium that plans to build a trans-Balkan oil pipeline from the Black Sea coast to the Adriatic or Aegean coast, and a bid in the tender for the privatisation of Romania's SNP Petrom.

Mining and metallurgy

The country has large deposits of lead-zinc ores, as well as some copper and chromium. Ferrous metallurgy contributes about 3 per cent to industrial production, and non-ferrous metallurgy contributes about 5.7 per cent. Much of the production is exported to the EU and to neighbouring countries. However, the large production of the metallurgical industry is currently under-utilised.

The loss-making Fenimak ferro-nickel plant is on the World Bank's list of large enterprises that must be sold or liquidated before World Bank credits can be disbursed. Feni was to be sold to Glencore (Switzerland), but following an audit carried out at World Bank insistence, in November 2000 it was sold for US$ 2.25 million to Societe Commerciale de Metaux et Mineraux (France), which will invest US$ 36 million over the next five years and retain all 880 employees. The French company has a contract to sell output to KruppThyssen of Germany. In recent years Fenimak has produced up to 5,000-6,000 tonnes of ferro-nickel per year, below its capacity of 7,000 tonnes per year. The French company is considering bringing an additional furnace into operation in 2-3 years.

Makstil is the country's largest steel producer and was formerly part of Rudnici i Zelezara Skopje. In December 1997 Duferco (Switzerland) acquired 54 per cent of Makstil from the previous shareholders for US$ 17 million and committed to modernise the works. The remaining shares in Makstil are owned by the three Macedonian investor companies, the Makedonija insurance company, Komercijalna Banka and employees. The EBRD made a US$ 15 million loan to Makstil in 1998, followed in October 2000 with approval of a working capital and guarantee facility of up to US$ 120 million to Duferco to provide guarantees for its operations in a number of countries. This includes a guarantee agreement for US$ 30 million for Makstil.

Seventy-four per cent of shares in the loss-making Jugohrom ferro-alloy plant are being sold at only DEM 2 million, compared with an original estimated value of DEM 51.2 million. An 82 per cent stake in the debt-ridden Bucim copper mining complex was sold in November 2000 for US$ 1.6 million on the local stock exchange. Mermeren Kombinat Prilep, the country's biggest marble producer, is to be sold to Kiriakidis (Greece).

Tourism

The country is spectacularly beautiful and attracts tourists from all over the former Yugoslavia as well as from Germany and Italy. The most popular tourist sites include Lake Ohrid, the national parks, the historic old towns and mountain ski resorts. The wars in former Yugoslavia and Kosovo discouraged tourism and visitor numbers have dropped dramatically.

Although there are currently only 85,000 beds, the country's tourist industry has considerable long-term potential, now that the regional situation is stabilising. Privatisation in the sector has been very slow, with the state postponing any large-scale sales for better times. There are plans to attract western investment into the sector over the longer term.

The World Bank is running a Community Development and Culture project, aimed at preserving architectural and artistic treasures of the Lake Ohrid region and increasing the tourism potential in an environmentally sustainable manner, at a cost of US$ 5 million under IDA terms.

Environment

Donors including the UNDP and USAID are providing assistance to the government to develop environmental management structures and are supporting the National Environmental Action Plan. With the assistance of bilateral and multilateral donors, air, water, and waste pollution issues are being addressed.

As a component of its Balkan Region Action Plan, the EBRD is developing a large municipal and environmental programme targeting urgent needs in the water and waste-water sectors. This water supply/treatment project, with a total cost of € 57.7 million, will cover up to five municipalities. (See *Case study* below.) The World Bank is also funding a Water Utility Improvement project to improve the operations of water and waste-water companies in Skopje, Bitola and Prilep. In Bitola and Prilep it will also finance the completion of the waste-water collection system and build waste-water treatment plants. The World Bank funding totals US$ 16 million.

Case study: Municipal Environmental Action Programme

In September 2000 the EBRD announced a loan of € 20.8 million towards a € 57.7 million programme to improve water and sewage infrastructure for five water companies servicing six cities. The financial package also includes € 31.8 million in grants and concessional loan financing from donor countries including Canada, Denmark, Germany, Greece, Japan, Portugal and Switzerland. Local contributions to the project amount to € 16.9 million. The Netherlands and Taiwan also contributed funds to prepare initial feasibility studies, and USAID will contribute by financing a public awareness programme.

This was the first infrastructure programme to get off the ground under the Stability Pact's "Quick Start" umbrella. The cities to benefit from the investment are Kumanovo, Ohrid/Struga, Stip, Strumica and Veles. Their water utilities will use the financing to address urgent shortcomings in the water and waste-water infrastructure, through rehabilitation and extension of distribution networks, water sources, water treatment plants, pumping stations, reservoirs and sewage systems. The project will lead to the creation of four vital waste-water treatment plants, in addition to the three existing ones, only one of which is in operation. It will also contribute to higher living standards for the local population, guaranteeing them a reliable supply of clean drinking water and reducing health hazards. At present water resources are too limited in the summer time to meet all agricultural and household needs.

The project also introduces commercialisation to the sector. It introduces cost recovery in the provision of municipal services, will strengthen the financial and operational performance of the water utilities, and will foster private sector involvement in contracting and construction management. It is also anticipated that it will have a demonstration effect, showing other water utilities the benefits of efficiency improvements resulting from commercialisation. Furthermore, it will introduce procurement procedures according to international standards, promoting a competitive market environment and contributing to transparency. The environmental improvements resulting from this project will also have benefit for the Vardar and Strumica rivers, and thus will have positive cross-border environmental impact downstream in Greece and Bulgaria. At present waste water largely reaches the rivers untreated, posing a high environmental and health risk.

Financial sector

The banking sector is entirely privately owned, but highly concentrated, with two dominant banks. Consolidation of the smaller banks is expected to follow from the raising of minimum capital requirements. New legislation and plans for further sector development are bringing regulations up to EU standards. The small stock exchange is gradually developing.

Banking sector

At the end of 2000, the share of total bank capital in the country that was privately owned had reached 100 per cent, with four majority foreign-owned and another six having varying degrees of foreign involvement. As at June 2000, there were 21 banks in the republic, a large number for a country with a population of 2 million and where financial intermediation is relatively low. The sector remains highly concentrated, with the two largest banks (Stopanska banka and Komercijalna banka) holding more than half of total assets and two-thirds of total deposits in the banking system. Many of the smaller banks are weak and some are unlikely to be able to meet the new capital requirements, scheduled for April 2001, of DEM 21 million for a full foreign operations licence, or even the lower requirement of DEM 7 million for domestic operations. Some of these banks are exploring merger possibilities.

The banking system suffers from a low level of public confidence, a high level of bad debts, a high cost of capital, poor allocation of credit and a lack of competition. New reform plans are set to address these problems.

Banking reform past and present

The privatisation of Stopanska banka (see below) marked an important step forward in bank restructuring and privatisation. In recent years the NBRM (the central bank) has strengthened the banking and legal regulatory system to meet international banking standards, with the aim of supporting economic reforms and the development of the market economy. This involved a wide-ranging recapitalisation operation carried out in 1995, transferring the bad assets of the 25 most indebted enterprises to a Bank Rehabilitation Agency, and increasing the supervisory activities of the NBRM. A new payments system is being introduced, supported by a Phare-sponsored project. Gradually, legislation is being further strengthened to improve supervision and consolidate the sector.

A **new banking law passed in July 2000** has led to significant changes in legislation. The law brings supervisory standards closer to EU standards and those recommended by the Basel Committee. In addition, it sets new frameworks for credit approval procedures and for strengthening corporate governance of banks. The new legislation will also allow foreign banks to establish branches and subsidiaries in the country.

Frozen foreign currency deposits

At the time of the dissolution of the former Yugoslav Republic, Macedonian commercial banks had large claims on the Yugoslav National Bank, which refused to return their foreign exchange deposits, causing the country liquidity problems and an inability to pay out retail foreign exchange deposits. Legislation was subsequently introduced to freeze these deposits, placing limits on their use, but providing a state guarantee for them. This had a bad effect on public confidence in the banking system at a time when high inflation was also undermining confidence in the national currency. Gradually the government has started to pay out the frozen deposits in instalments, and they are also acceptable as payment in privatisation transactions. A new Law on Frozen Foreign Exchange Savings Deposits was enacted in 2000 to address the issue of servicing frozen foreign deposits within a fiscally sustainable framework. It is anticipated that this move will help to improve savers' confidence in the banking system. The issue affects about 200,000 savers who are owed DEM 1.2 billion.

Within the reform programme outlined in autumn 2000 the Finance Minister identified development of the banking system as a priority, including introduction of an up-to-date system to perform effective allocation of financial resources, strengthening and promoting competition in the banking system by giving incentives to the entrance of foreign banks, a high level of liberalisation in foreign exchange operations, and increased domestic savings as a condition for higher investment. The programme anticipates another new banking law in full compliance with EU directives and international accounting standards. The deposits insurance system is to be upgraded and the supervision standards of the NBRM are to be fully aligned with Basel principles, as well as strictly applied. New laws on foreign exchange, foreign trade operations and foreign credit relations are to be prepared.

Banking privatisation and mergers

The full privatisation of the largest bank in the country, **Stopanska banka** (SB), was completed in April 2000. The strategic investor is the National Bank of Greece, which now holds 70 per cent of the capital of the bank. The EBRD and IFC each hold a 12 per cent stake. Before privatisation, SB was forced to provision heavily against bad loans, due to its large exposure to loss-making companies. Under the privatisation agreement, the four largest exposures have been removed from its books and replaced with government bonds. In July 2000 the bank's Board announced that recapitalisation by DEM 50 million (US$ 23.7 million) had been successfully completed. The presence on the investment market of a strong, fully capitalised, foreign-run bank is a major advantage for the economy.

A 65 per cent stake in **Kreditna banka**, the country's fourth largest, was bought by Alpha Credit Bank (Greece) for DEM 18.4 million in 2000. **Komercijalna banka**, the second largest in terms of assets, is fully private, with the EBRD holding a 5 per cent stake. It offers an attractive prospect for foreign investors in view of its stable financial results and a good investment portfolio. In October 2000 Nova Ljubljanska banka (NLB, Slovenia's largest bank) bought a 25 per cent stake in **Tutunska banka**, the country's third largest bank, on the Macedonian stock exchange for US$ 2.7 million. In December Germany's LHB Internationale Handelsbank, which is a member of the NLB group, bought a further 25.2 per cent stake for DEM 15 million, making it joint majority owner with NLB. Tutunska banka is a medium-sized commercial bank that has traditionally specialised in servicing the tobacco industry.

In April 2000 the EBRD approved an equity investment of up to DEM 6 million through a capital increase in the **Export and Credit Bank** (ECB), which had previously participated in its SME credit line (see below). The capital increase will allow the bank to become an active participant in the consolidation of the banking sector and to develop into one of the main providers of retail banking services. It will also make it attractive to a foreign strategic investor.

Apart from the foreign presence established through privatisation, there are two foreign branches, Ziraat Bank of Turkey and Balkanska Banka of Bulgaria.

The gradual raising of minimum capital requirements is expected to lead to consolidation of the banking sector. From April 2000 they were raised to DEM 18 million, rising to DEM 21 million from April 2001.

Non-bank financial institutions

The Stock Exchange (MSE) was founded in late 1995 as the first organised bourse in the history of the republic. A joint stock company, it first opened for business on 28 March 1996 and trades stocks and bonds, but remains under-developed. It is represented on the Federation of Euro-Asian Stock Exchanges (FEAS) in Istanbul, Turkey, and is governed by a Law on Issuances and Trading Securities adopted in 1997 which established a regulatory framework for the securities market and a Securities and Exchange Commission are regulator and supervisor.

The MSE initially had 17 members, of which 13 were banks, two savings houses and two insurance companies. Following the 1997 Law, its members may only be brokerage companies solely active in trading in securities and licensed by the Commission. At the start of 2001 there were eight such brokerage firms. The MSE operates on a non-profit basis and has a founding capital of DEM 1 million.

There are three tiers on the MSE: the first tier lists blue-chip companies with a market capitalisation of at least DEM 15 million, the second has less strict listing requirements (capitalisation of at least DEM 1 million), while the third operates, in effect, as an OTC market. Most activity takes place on this market, as the only requirement for participation is the submission of the latest financial statement of the issuer.

Turnover on the MSE intensified in September 2000 after a four-month decline to reach a total of MKD 434.2 million (about DEM 15 million). The largest share of turnover (82.3 per cent) was realised on the unofficial market. There was an increase in trading on the first tier of government bonds issued against frozen household deposits (see above). Total turnover for the period from January to the end of September 2000 was MKD 5,639.9 million, roughly DEM 200 million. Plans to expand the market include proposals for a law on investment funds, a clearing house and a central share registry.

Selected sources of financing for SMEs

Support for the development of SMEs is a government priority. The Finance Minister has proposed to the NMB that compulsory foreign-currency deposits for exporters be reduced from 100 to 40 per cent in order to free money for credits to SMEs. Tutunska banka has reduced interest rates for enterprise loans to 13-17 per cent, below its main competitors, Komercijalna banka (15-20 per cent) and Makedonska banka (14-22 per cent). However, credit remains expensive because of the high degree of risk resulting from the state of the economy.

A number of initiatives have been established by international financial institutions and other donors. These include the following funds.

Credit lines

The **EBRD SME credit** line is channelled through five participating local banks. The initial credit lines extended in December 1995 were all well utilised except for one which disbursed only slowly, with a total of 70 sub-projects extended in total. Following the success of the first credit lines, EBRD extended a second set of five-year credit lines in November

1996. The total amount is DEM 45 million (Stopanska banka DEM 15 million, Makedonska banka DEM 15 million, Export-Import banka DEM 6 million, Almako banka DEM 6 million, Export and Credit banka DEM 3 million). The credit line is sovereign guaranteed, with a price to participating banks of 3.2 per cent over LIBOR. By March 2000, 87 per cent had been disbursed. The lines have supported 110 sub-projects so far, with an average sub-loan size around DEM 300,000. Before the extension of the first EBRD credit line, capital investment was being financed by revolving short-term loans at interest rates exceeding 15 per cent.

Under the **World Bank's Private Sector Development Programme**, two credit lines have been opened: the first in 1996, worth DEM 18 million (now fully disbursed), and the second in 1997 worth DEM 45 million (about one-third disbursed by autumn 2000). The average sub-project in industry is DEM 800,000 to 1 million, and in agriculture DEM 60,000 to 100,000. The credit lines have an APEX structure with the central bank, and local banks are fully responsible for sub-loans.

In spring 1998, **Phare** initiated a **micro-lending programme** with DEM 6.2 million. The participating banks supply matching funds. Phare guarantees two-thirds of the risk. The maximum loan for a sub-project is DEM 40,000. The programme is managed by the National Enterprise Promotion Agency. The executing organisations are the European Savings Bank Group, Lloyds Bank and the German Savings Banks Foundation for International Co-operation. The micro-credit scheme is administered through a network of eligible local banks (Komercijalna banka, Stopanska banka, Tutunska banka, Ohridska banka and Rodobanka) which have been approved for handling credit lines. Targets are micro and small enterprises; trade finance and primary agriculture are excluded. Phare is also providing technical assistance funds, which target improved and faster decision making in processing credit applications. In November 1999 a further € 3.7 million funding was approved to supplement the micro-credit scheme.

USAID has provided support for the non-governmental organisation, Moznosti, a 100 per cent grant-financed **micro-credit institution**. It has also initiated a pilot programme for group lending. The main sectors under this programme are services, manufacturing and agriculture. The UK Know How Fund has set up **SME Support Agencies** in three regions, with Dutch government co-financing.

Germany's development agency **Kreditanstalt für Wiederaufbau (KfW)** has introduced a start-up assistance programme worth DEM 10 million for returning refugees and migrants to the country. The maximum loan for a sub-project is DEM 150,000 (exceptionally DEM 250,000 will be considered). KfW has also contributed to the establishment in 1998 of the Macedonian Development Bank (MDB).

In September 1999 the government of **Taiwan extended three credit lines** under favourable conditions for Macedonian companies. The first credit line, totalling US$ 3.5 million, targets SMEs which need to borrow in order to purchase equipment and materials. The second line, worth US$ 12 million, targets housing construction and the third targets the construction of sports halls in schools. The agreement for the first loan of this line, worth US$ 20 million, was signed in the second half of 1999. The NMB selected nine private banks to manage the credit lines.

The **South-East Europe Enterprise Development** (SEED) is an IFC initiative designed to support the development of SMEs in south-eastern Europe (this country and also Albania, Bosnia and Herzegovina, and Kosovo). By December 2000 funding commitments totalled US$ 20 million, with a further US$ 13 million to be secured over the five-year life of the programme. The IFC is providing funding and also the management team to implement the SEED. Main aims include outreach to regional investment funds for potential pipeline development, investment preparation and post-financing services, creation of business centres to support Internet-based learning among SMEs and their support institutions, development of advocacy groups for SMEs, local training and technical assistance towards developing a local consultancy capacity for SMEs, and development of enterprise zones, and leverage of undisbursed international funds towards SME development. In the republic, the SEED will support the development of a one-stop service within a government agency or business centre to provide relevant information for firms wishing to export. There are plans to develop a central Macedonian business directory, both in hard copy and on the Internet, and the SEED would support it in order to ensure the full inclusion of SMEs. Other possible areas identified for the SEED's involvement are modification of legislation and training related to bad loan workout, reform of banking laws to enable micro-banks to enter the market, and helping the Ministry of Finance to collect macroeconomic information on SMEs.

Equity finance

The **Small Enterprise Assistance Fund** (SEAF) is a fund established in 1999 of US$ 13 million for equity and quasi-equity investments in SMEs. Investors include the EBRD, with participation of US$ 4 million (30.77 per cent), the IFC (US$ 2.5 million), DEG (US$ 2.5 million) and USAID (US$ 4 million). Target sectors are agribusiness, food processing, tourism, light manufacturing and community services. The SEAF will take significant minority stakes typically representing between 25 per cent and 49 per cent of the investees' total capital, but will generally not take management control of any investee company. By March 2000, 69 prospective portfolio companies had been reviewed, out of which 21 were in the pipeline while 48 had been rejected. Two investments had been made: DEM 450,000 equity plus debt financing to a producer of household cleaning products and DEM 630,000 to the publisher of the newspaper having the largest circulation in the country.

Another fund is currently under development, also targeting the SME sector. The **Macedonia Equity Fund** (MEF) is to be established with a total capital of US$ 15 million, of which US$ 6 million will be contributed by the EBRD and US$ 9 million by the Taipei China International Co-operation Development Fund (ICDF). Of the ICDF's contribution, US$ 6 million is for investment while the remaining US$ 3 million is to pay for establishment and fund manager fees for the fund. MEF will make equity and quasi-equity investments in Macedonian private SMEs. The equity would finance capital expenditure programmes and working capital requirements of investee companies. The MEF's principal investment objective is to achieve long-term capital appreciation by contributing to the modernisation, expansion, restructuring and development of small and medium sized privatised and private enterprises in Macedonia, through equity investments in commercially viable companies and projects. The MEF is to take significant minority stakes in the portfolio companies and to influence the management and operations of portfolio companies through direct representation on the portfolio company board.

The EBRD is also developing a **small equity fund** with US$ 9 million identified in co-financing from bilateral donors. This fund will target small companies with equity participations as small as US$ 50,000-100,000. It will take significant minority stakes in the portfolio companies through negotiated transactions and will have an active role in influencing their operations and management.

EBRD Trade Facilitation Programme (TFP)

The EBRD runs a successful regional trade facilitation programme providing trade guarantees for exporters and importers in all its countries of operations. This greatly benefits SMEs by allowing them to finance imports of necessary materials and goods without having to pay cash up front. On behalf of their clients, local issuing banks can apply to the EBRD for guarantees for their letters of credit to confirming banks representing their clients' trade partners.

For example, if a company in a country of operations wishes to import goods from a foreign company, but is obliged to provide either cash on delivery or a letter of credit confirmed by an international bank and guaranteeing payment for the goods, it can apply to its local bank to issue the letter of credit. If satisfied with the importer's ability to pay the credit back within a set period, the bank will issue the letter of credit. In order to avoid having to pay cash up front and thus reduce its own liquidity, the local bank can apply to the EBRD for a guarantee for the letter of credit. This provides the exporter's bank with full risk coverage, and gives it the assurance needed to confirm the letter of credit and enable the transaction to go ahead.

The TFP is designed to be flexible to suit a variety of circumstances and to offer a fast and simple transaction approval process.

In addition to off-balance-sheet credits, it provides short-term revolving loans to the local banks for pre-export finance on-lending to local SMEs. All trade finance lines provided to the issuing banks are unsecured and uncommitted, meaning that they can be amended or cancelled by the EBRD at any point, but also that no commitment or front-end fees are charged to the issuing banks. Over 125 international confirming banks have joined the programme, giving worldwide coverage and a strong business development tool for those involved.

Five Macedonian banks have qualified for trade finance lines under the TFP, Export-Import banka, Komercijalna banka, Stopanska banka, Tutunska banka and the Export and Credit Bank. The Macedonian experience of the TFP has been exemplary. Komercijalna banka has been an especially successful and supportive user of the TFP, and by January 2001 had applied for over 70 guarantees worth a total of € 10.3 million for a wide range of companies in sectors including pharmaceuticals, construction materials, metallurgy, agricultural inputs and machinery, food products, white goods and many others. The size of the credits guaranteed through Komercijalna banka ranges from € 1.5 million to under € 10,000. The total value of credits guaranteed for Macedonian issuing banks at the beginning of 2001 was € 22 million.

EBRD activities

EBRD operations in the country grew significantly during 2000. As at 31 December 2000, the European Bank for Reconstruction and Development (EBRD) had signed 16 projects in the country, with commitments totalling € 292.6 million in support of projects with a total cost of € 621.4 million. Of these, 11 are in the private sector and five in the public. More specifically, seven fall in the critical infrastructure sector (telecommunications, power, air transport and municipal services), six in the financial sector and three in the private corporate sector.

Overview of EBRD activities and key objectives

In response to the challenges facing the country, and to build on its earlier activities, the EBRD has identified the following strategic priorities:

- **Small business and micro-finance**
  The Bank will continue to be responsive to the financing needs of small and micro businesses by working with existing financial intermediaries and, where appropriate, through the establishment of new intermediaries. Work on improving the investment climate and with other support groups for small and medium-sized enterprises (SMEs) will complement EBRD financing.
- **Bank privatisation and sector consolidation**
  The EBRD is contributing substantially to banking sector reform through an investment in the full privatisation of Stopanska Banka, the country's largest bank. Additional support for the banking sector in the context of sector consolidation will be considered.
- **Increasing direct interventions in the corporate sector**
  The Bank will continue to focus on direct loans and investments in selected private companies, aiming to further enhance investor confidence and regional integration. Policy dialogue will focus on improving the investment climate and promoting good corporate governance.
- **Private and commercial infrastructure**
  The country has reached a stage in its transition where private project finance opportunities may be considered in the power and telecoms sectors. The continued policy dialogue on the establishment of an acceptable regulatory framework in each sector is planned. The EBRD will continue to finance public infrastructure when it assists private sector development, but preference will be given to private infrastructure.
- **Developing and modernising municipal infrastructure**
  The EBRD has recently signed and is now beginning implementation of its first municipality-based project in the country, a water supply/treatment project covering six municipalities. The Bank has identified grant and concessionary funds to blend with EBRD financing.

While targeting these objectives, the Bank will continue liaising closely with other international financial institutions (IFIs) to ensure complementarity in the provision of project financing and consistency in policy dialogue.

Signed projects as at 31 December 2000

Infrastructure

MEAP Water Supply/Treatment Programme

In September 2000, the EBRD extended a sovereign loan of € 20.8 million to be on-lent to five Macedonian water utilities financing investments in the construction, rehabilitation and extension of water and waste-water infrastructure. The five water companies are serving the municipalities of Kumanovo, Ohrid/Struga, Stip, Strumica, and Veles. In addition, international grants and concessional loans of € 31.8 million and local contributions of € 5.1 million will be provided. Investment grants/concessional loans are being provided by Germany, Greece, Portugal and Switzerland. The total project investment cost is € 57.7 million.

The project aims to improve the quality and reliability of water supply, reduce health hazards and pollution of surface water from discharging untreated waste water and strengthen the financial and operational performance of the water utilities involved.

Emergency GSM Extension and Network Modernisation Project

In October 1999, the EBRD extended a loan of € 18.7 million to Makedonski Telekomunikacii, the state-owned company that provides telecommunications, data and mobile phone services. The loan will enable the company to double its mobile GSM network capacity and to modernise its information systems. This project is a component of the EBRD South-Eastern Europe Action Plan, within the short-term response plan for assisting local infrastructure development. This is the first EBRD loan extended to a state-owned Macedonian company without a sovereign guarantee.

Skopje Airport Upgrading Project

In December 1995, a loan of DEM 17.8 million was extended for an urgent safety-related upgrade of Skopje Airport. The main objective of the project was to ensure that safe and efficient air links were maintained within the country. The loan has helped to improve the runway, taxiways and the lighting system so as to optimise the airport's capacity. It is helping the aviation authorities to maintain the improved facilities and to plan the airport's long-term development. Project preparation was funded by Canadian technical co-operation funds of US$ 230,000, and the US Trade and Development Agency funded the preparation of the airport development plan to the extent of US$ 150,000. The loan was sovereign guaranteed.

Macedonian Telecommunications Project

A loan of US$ 42.55 million was signed in March 1995 to modernise the local, long-distance and international telecommunications network. The objective was to connect about 78,000 new subscribers to the fixed telecommunications network and to provide digital exchanges that give commercial entities access to modern, high-quality services nationally and world-wide. A complementary technical assistance component assisted the Public Enterprise for PTT Traffic, "Makedonija", to develop a corporate strategy and prepare for future privatisation. The loan was sovereign guaranteed.

Air Navigation Systems Upgrading

In October 1994, the EBRD provided financing of US$ 14.05 million to upgrade air navigation equipment and to provide comprehensive air navigation services to commercial aircraft flying in the country's airspace. The total project cost was US$ 17.4 million, 80 per cent of which was financed by the EBRD. The US Trade and Development Agency provided US$ 250,000 in grant funds for air traffic controller training and project implementation assistance. The loan was sovereign guaranteed.

Power Sub-Sector Project

In December 1993, the EBRD extended a loan of DEM 46.5 million to Elektrostopanstvo na Makedonija, the national power corporation. DEM 38.4 million financed the construction of a 113.5-kilometre transmission line between Bitola Thermal Power Station and Skopje, the main industrial centre. The balance was allocated to support the government's Energy Conservation Programme. The loan was sovereign guaranteed.

Financial Sector

Stopanska Banka (SB)

SB, the largest bank in Macedonia, is in the process of being privatised with the National Bank of Greece (NBG) taking a majority stake in the bank. The EBRD and the IFC are jointly co-investing with NBG. In December 1999, the Bank and the IFC agreed to purchase existing shares and to subscribe to new shares for a total of up to € 9.2 million each. The EBRD will then have a stake of up to 10.5 per cent in SB. The capital infusion will permit further asset growth and the implementation of SB's investment programme that includes modernisation of its computer systems, branch network upgrading and personnel training.

Komercijalna Banka A.D.

In March 1996, the EBRD extended financing totalling DEM 15 million to Komercijalna Banka A.D., (equity participation and convertible loan), for on-lending to private sector clients and to assist the bank to upgrade its operations and especially to improve its information technology, management information systems and branch network.

Export & Credit Bank (ECB)

In May 2000, the EBRD invested € 3.1 million in ECB's equity and acquired a 31 per cent stake. The investment was made with the objective of developing Export & Credit Bank into a strong medium-sized bank, with focus on the SME and retail sectors. In parallel, the EBRD has mobilised TC funds and appointed two banking experts to assist ECB.

SME Credit Lines

In December 1995, the EBRD extended credit lines to five local banks for medium and long-term financing of private small and medium-sized enterprises. The total credit line was DEM 40 million, with DEM 10 million allocated to Makedonska Banka A.D., DEM 15 million to Stopanska Banka A.D., DEM 6 million to Almako Banka A.D., DEM 6 million to Export-Import Banka A.D, and DEM 3 million to Export and Credit Bank. The loan facility is sovereign guaranteed.

SEAF Macedonia

In July 1999, the EBRD took a US$ 4 million equity participation in SEAF-Macedonia LLC, a US$ 13 million venture capital fund. Follow-on investments range between US$ 400,000 and US$ 1 million. The fund makes equity and quasi-equity investments in small and medium-sized local companies. It is managed by the Small Enterprise Assistance Fund.

Trade Facilitation Programme

In January 1999, the EBRD launched its new Extended Trade Facilitation Programme (TFP) covering its 27 countries of operations. This programme facilitates intra and extra-regional trade by guaranteeing local enterprises' letters of credit in connection with export and import transactions. Originally the Trade Guarantee facility was extended to three local Macedonian banks, Stopanska Banka, Komercijalna Banka and Export-Import Banka. In 2000 two other banks joined the programme, namely Tutunska Banka and Export Credit Bank. As at 31 December 2000 commitments exceeding € 22 million had been guaranteed.

Private Corporate Sector

Duferco-Makstil WC Facility

In December 2000 the EBRD signed the regional "Duferco Working Capital and Guarantee Facility" Agreement, under which the Bank agreed to guarantee against specified events, existing working capital lines for pre-defined amounts and steel plants in eastern Europe. The ceiling for this working capital facility is set at US$ 120 million, of which up to US$ 30 million is allocated to Makstil AD, a Macedonian steel producer, majority owned by the Duferco group.

Thessaloniki – Skopje Crude Oil Pipeline

On 19 December 2000, the EBRD approved a US$ 50 million (€ 59 million) senior loan for the construction of a new 221-kilometre crude oil pipeline, linking the Greek port of Thessaloniki and the OKTA Refinery in Skopje. The pipeline, which will carry up to 2.5 million tonnes of crude oil and petroleum products per year, will reduce current transportation costs and secure long term supply of oil to the country. The total project cost is US$ 105 million (€ 122 million). Hellenic Petroleum, the largest industrial company in Greece, together with Aegek, a Greek construction group, is contributing US$ 55 million.

The pipeline also provides a more environmentally sound alternative to the current road and rail transportation.

Alkaloid A.D.

In July 1999, the EBRD extended a loan of € 8.7 million to Alkaloid A.D., a locally owned and managed company. The project was financed jointly with the IFC, which invested a further € 8.7 million. The loan will be used to upgrade, expand and modernise Alkaloid's Skopje pharmaceutical plant and to assist the company in meeting "qualifying for good manufacturing practice" (GMP) standards.

Makstil A.D.

In October 1998, the EBRD extended a US$ 15 million loan to assist Makstil, a recently privatised steel producer acquired by Duferco of Switzerland, with its expansion programme. The loan is being utilised to modernise Makstil's casting facilities and its Skopje plate mill plant to restore integrated production capacity, thus increasing the plant's overall efficiency.

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Signed projects as at 31 December 2000 (in € million), exchange rates as at 31 December 2000

Operation name	Sector	Total cost	EBRD debt	EBRD equity	EBRD total
Private					
Komercijalna Banka	Finance	7.7	5.0	2.7	7.7
SME credit line	Finance	18.5	18.5	0	18.5
SEAF Macedonia	Finance	14.0	0	4.3	4.3
Stopanska Banka A.D., Skopje	Finance	77.0	9.4	0	9.4
Export and Credit Bank	Finance	3.1	0	3.1	3.1
SME Export and Credit Bank	Finance	1.5	1.5	0	1.5
Trade Facilitation Programme:	Finance		0.2		
Export-Import Banka		2.8			2.2
Komercijalna Banka		0.7			4.8
Stopanska Banka, Skopje		2.9			3.2
Tutunska Banka AD Skopje		0.1			0.2
Export and Credit Bank (ECB)		0.6			0.6
Thessaloniki-Skopje crude oil pipeline project	Pipeline infrastructure	112.8	53.7	0	53.7
Alkaloid-AD	Pharmaceutical	35.4	8.7	0	8.7
Makstil	Primary metal manufacturing	75.2	16.1	0	16.1
Duferco – Makstil Facility	Primary metal manufacturing	32.2	32.2	0	32.2
Emergency GSM extension and network modernisation programme	Telecommunications	18.7	18.7	0	18.7
Sub-total		***403.2***	***174.7***	***10.1***	***184.8***
Public					
Power sub-sector project	Power and energy	33.4	17.3	0	17.3
Macedonian telecommunications project	Telecommunications	88.0	45.6	0	45.6
Air navigation system upgrading	Transportation	25.2	15.1	0	15.1
Skopje Airport rehabilitation	Transportation	13.9	9.0	0	9.0
Municipal environmental action programme	Water and sewage	57.7	20.8	0	20.8
Sub-total		***218.2***	***107.8***	***0***	***107.8***
Total		**621.4**	**282.5**	**10.1**	**292.6**
of which private					63.2%
of which public					36.8%

Notes